

CALIFORNIA DEPARTMENT OF FOOD AND AGRICULTURE
AUDIT OFFICE



TM

LODI-WOODBRIDGE WINEGRAPE COMMISSION
AUDIT REPORT #08-083

LODI-WOODBRIDGE WINEGRAPE COMMISSION
AUDIT REPORT

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Mr. Robert Maxie, Branch Chief
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California Department of Food and Agriculture
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The California Department of Food and Agriculture (CDFA), Division of Marketing Services, Marketing Branch, requested the Audit Office perform a limited scope fiscal and compliance audit of Lodi-Woodbridge Winegrape Commission (Commission.) The objective of this audit was to determine whether certain activities and expenditures incurred by the Commission comply with the law and are within Board authority. In addition, our office was to identify any internal control weaknesses we noted upon examination of the Commission's financial records.

The audit scope was limited by the Marketing Branch as it related to certain expenditures. Most notably, the Marketing Branch has allowed the State's marketing orders to implement a travel policy that can be applied retroactively to the audit period. This travel policy allows for the State's marketing orders to incur lodging and per diem expenses up to three times the current State rate. Therefore, our office has been instructed to report only amounts that exceeded this threshold.

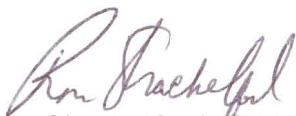
Furthermore, our audit scope was limited to the fiscal years 2006, 2007, and 2008. Although the scope was limited to these three years, our office expanded the scope to include information that covered other years if it was readily accessible and/or may have assisted us in understanding a particular issue.

To accomplish the overall audit objectives, our audit methodology consisted of, but was not all inclusive of, the following review of the Commission's:

- Compliance with various rules and regulations
- Employee and Policy Manuals
- Internal controls
- General ledger detail and various financial related documents
- Board and Committee minutes
- Expenses and supporting documentation, including credit card statements and corresponding receipts for each charge
- Contracts
- Research grants
- Payroll documents

We conducted our audit in accordance with Generally Accepted Government Auditing Standards, issued by the Comptroller General of the United States.

This audit report is intended solely for the information and use of the management of the CDFA and Commission and should not be used for any other purpose.



Ron Shackelford, CPA
Chief, Audit Office
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EXECUTIVE SUMMARY

The California Department of Food and Agriculture (CDFA), Division of Marketing Services, Marketing Branch, requested the CDFA Audit Office to perform a limited scope fiscal and compliance audit of the Lodi-Woodbridge Winegrape Commission (Commission) to determine whether certain activities and expenditures incurred comply with the law and are within Board authority. In order to accomplish this, our primary focus was the Commission's expenses and compliance with various rules and regulations. We noted the following administrative weaknesses:

- A review of the Commission records identified internal control weaknesses in the relationship between the Commission and the California Wine Education Foundation (Foundation). These entities are separate from each other and maintain separate books and records. Our review of the Commission's books and records identified several issues that raise concerns over the Commission accurately accounting for and reporting expenses, and the appearance of clear separation between the entities. The Commission has two contracts with the Foundation: an administrative services contract and a sublease. The Commission does not appear to be compliant with both contracts. For instance, the Commission has not fully recovered all its administrative expenses from the Foundation. There are expenses associated with providing services to the Foundation that were not recovered or identified. Additionally, there was a lack of supporting documentation for the methodology applied in the determination of the allocation rate when charging for shared expenses. Some accounting transactions also lacked supporting documentation. Also, the direct expenses the Commission paid to the Foundation upfront were not always reimbursed because these expenses were not clearly identified as Foundation expenses. These expenses remained in the Commission's financial records. Furthermore, the Commission does not require the Foundation to provide an accounting for the Commission's its monetary contributions to the Foundation to ensure the contribution was used to further the Commission's mission.
- The Commission did not establish a written contract with the Lodi Conference and Visitors Bureau (Visitors Bureau) and there was not adequate supporting documentation for us to determine how the allocations for the reimbursement of the shared expenses were determined. Without clear supporting documentation, we are unable to determine whether the allocation was reasonable based on the data used. Furthermore, in fiscal year 2005/2006, the Visitors Bureau incurred shared expenses, including rent, from December 2005 through May 2006 and the Commission did not seek reimbursement for the rent. Eventually, the Commission absorbed all of these shared expenses.
- A review of the expenditures revealed a lack of documentation for credit card expenses, non-wine alcohol purchases that do not appear to further the Commission's mission, and lack of a thorough review of expenses. For the three-year period

audited, our office noted \$32,948 of \$71,451, or 46% of expenses charged to the credit card were not adequately supported with receipts and/or justifications. These expenses exceeded the Commission's travel policy of providing support for expenses in excess of \$25. Additionally, we noted instances when there was no recipient listing, business purpose, and itemized receipt for restaurant charges. An itemized receipt provides transparency as to the nature of the expense. Additionally, we noted instances when non-wine alcohol purchases were made, with no documentation evidencing that these purchases further the mission of the Commission. Furthermore, the Commission did not thoroughly review expenses prior to payment, which resulted in double payments.

- The Commission does not have adequate internal controls over their wine inventory. As a result, the Commission does not have knowledge of the value of the inventory, number of bottles of wine purchased or received into the inventory, and the number of bottles of wine the Commission donated, exposing the Commission to a loss. Additionally, there is no assurance that all the wine was either donated or used for purposes that may benefit the Commission, since the recipient, purpose, and value of the donation were not always documented.
- Wine was gifted to employees for special occasions, such as birthdays and as farewell gifts. State law requires public money to be used to further a department's mission. Gifts to employees do not appear to further the mission or benefit the Commission and therefore may be prohibited.
- The Commission failed to enter into written contracts for some service agreements. The Commission paid for services for, but not limited to, design for artwork, advertising, guides, maps, signage, newsletters publications, and event planning. There was no written contract between the Commission and the individuals or companies for these services to outline the term of performance, payment, and scope to mitigate any possible disputes.
- The Commission does not have proper accountability over its research grants. The funding paid is based on an invoice, and the final payment is paid when the final research report is completed. The Commission does not require the grantees to provide progress reports or a final accounting over the grant money awarded them to ensure that the funds were used for the intended purpose.
- The Commission has not accounted for or reported the value of the employees' use of the Commission's vehicles as a fringe benefit.

KEY RECOMMENDATIONS

1. *The Commission should examine and revise its procedures to ensure there is clear separation between the Commission and the Foundation, in fact and appearance; and ensure commingling of funds does not occur.*
2. *The Commission should ensure that it is in compliance with its contracts between itself and the Foundation. If necessary, the contracts should be reviewed and amended.*
3. *The Commission should review the costs associated with providing services to the Foundation and adopt a full cost recovery policy to ensure its full costs are recovered when performing services for the Foundation.*
4. *The Commission should require its employees to maintain detailed time records that specifically identify the amount of time its employees spend performing Foundation activities in order to ensure the commingling of costs does not occur and to promote accuracy of the Commission's financial statements.*
5. *The Commission should maintain documentation demonstrating its analytical process and justification for using estimated data instead of actual data.*
6. *The Commission should ensure that it retains supporting documentation for all accounting transactions.*
7. *The Commission and the Foundation should ensure the direct expenses of each entity are properly recorded in each separate entity's accounting records. If necessary, a policy should be developed to identify events, as either a Commission or Foundation activity.*
8. *The Commission should seek reimbursement from the Foundation for any of the expenses that were not repaid to the Commission.*
9. *The Commission should have the Foundation provide a full accounting for the \$28,000 "loan" that the Commission later noted as a contribution for Zinfest, to ensure all expenses further the mission of the Commission. Furthermore, the Commission should consider requiring recipients of large contributions to provide an accounting of the money to ensure it furthers the Commission's mission.*
10. *The Commission should consider establishing an accounts receivable for any unpaid amounts due and also ensure all business relationships are solidified in written contracts identifying the parties involved, terms for the performance, payment, and scope, and signed by both parties.*
11. *The Commission should maintain documentation demonstrating its analytical process and justification for determining the cost allocations between the Commission and the Foundation. Our office encourages the use of actual data to determine the allocation in order to provide a more accurate allocation.*
12. *The Commission should ensure employees with a Commission issued credit card are required to support all charges incurred, including business meals, with an itemized*

receipt. The receipt should be maintained within the credit card file along with documentation listing the guests who attended and the business purpose of the meal.

- 13. The Commission should incur expenses only necessary to support its mission.*
- 14. The Commission should maintain itemized receipts for all expenses to ensure expenses are adequately supported.*
- 15. The Commission should thoroughly review expenses prior to payment to avoid potential overpayments.*
- 16. The Commission should review employee travel claims prior to reimbursement to ensure the claim complies with the Commission's travel policy.*
- 17. The Commission should establish policies and procedures for its wine inventory to ensure proper valuation and documentation of the use of the wine inventory. The documentation of the use of the wine inventory should include the recipient, purpose, and valuation of the donation provided.*
- 18. The Commission should not pay for any invoice from the Visitor Center unless accompanied by a detailed receipt to ensure the purchase was indeed from a Commission employee and for a purpose that would further the Commission's mission.*
- 19. The Commission should be cautioned that gifts of public funds are prohibited.*
- 20. The Commission should ensure all services are properly bid and have written contracts that identify the parties involved; outline the terms for performance, payment, and scope; and are signed by both parties to mitigate any disputes.*
- 21. The Commission should improve its internal controls over grant awards by requiring grantees to provide additional financial information, such as progress reports and a final accounting of expenses applied against the grant. The purpose of these reports is to improve the Commission's monitoring of grant awards and provide more transparency over actual expenditures billed by researchers to the grant contract.*
- 22. The Commission should ensure that it is accounting for and reporting the income for the personal use of the Commission's vehicles by the two employees and determine whether the methodology complies with the IRS criteria in valuing the personal use the Commission's vehicle.*

REPORTABLE FINDINGS

RELATIONSHIP WITH THE CALIFORNIA WINE EDUCATION FOUNDATION

A review of the Commission records identified internal control weaknesses in the relationship between the Commission and the California Wine Education Foundation (Foundation), a 501(c) (3), non-profit public benefit corporation. These entities are separate legal entities and maintain separate financial records, but have the parallel purposes of maintaining and promoting the Lodi-Woodbridge winegrape industry. Although the California Food and Agricultural Code Section 74901 allows the Commission to make contributions of funds for purposes of maintaining, promoting, and enhancing the Lodi winegrape industry, the internal control weaknesses identified in this report limit the Commission's ability to ensure that all of its funds were spent for proper purposes.

Our review of the Commission records identified issues with contract compliance, full cost recovery, clear documentation for allocations and accounting transactions, reimbursements of direct Foundation expenses the Commission paid upfront, and accounting for monetary contributions to the Foundation. As a result, we are concerned about the Commission accurately accounting for and reporting expenses, and the appearance of clear separation between the entities.

Contracts and Full Cost Recovery

The Commission does not appear to be in compliance with two contracts that were entered into between the Commission and the Foundation. One contract was for administrative services while the other was a rental contract.

The first of these contracts is an administrative services contract. Since February 2000, the Commission has been contracted to perform administrative and management services for the Foundation, whose purpose is to support education and research related to the Lodi and greater California wine and winegrape industries. These services include the day-to-day operations of the Lodi Wine and Visitor Center (Visitor Center), and organizing the Foundation's annual event, Zinfest.

According to the contract, the Foundation is to pay "reasonable administrative fees as determined on an annual basis by the parties." However, it does not appear that the full administrative fees were paid to the Commission. Based on our review of the Commission's expenses and accounts receivable for the Foundation, the Commission pays for all expenses upfront, calculates the allocation the Foundation owes, and then invoices the Foundation. The expenses include, but are not limited to, salary and payroll expenses for the Visitor Center manager and staff, rent, utilities, office supplies, postage, and copier lease. There were other expenses associated with providing services to the Foundation that were not recovered or even identified. For instance, the time spent by Commission employees providing services to the Foundation, such as bookkeeping, maintaining records, and

organizing Foundation functions, such as Zinfest, were not tracked or considered when calculating the allocation.

We further noted that Commission employees spent a considerable amount of time planning and promoting Zinfest and these employees were provided with bonuses or gift cards for their efforts. We noted for the 2006 Zinfest, three Commission employees received a total of \$3,911 in compensation, based on the percentage of sponsorships received. Approximately \$81,000 was received in sponsorships. The bonus checks were written from the Commission bank account to the employee and then the Commission invoiced the Foundation for the expenses. Then, for the 2008 Zinfest, we noted that seven Commission employees and one Visitor Center employee received \$100 gift card each, as an appreciation gift. These instances further identify the commingling of employee hours between Commission and Foundation activities. Therefore, it appears the Commission may not be accurately reporting expenses.

There is further concern with whether the individuals the Commission considers to be "Foundation employees" are indeed Foundation employees. Based on the Commission's criteria the "Foundation employees" only work for the Visitor Center and do not do any work for the Commission. These employees' salaries and benefits are paid by the Commission upfront and then the Commission receives a reimbursement for them. Although these employees are ultimately paid by the Foundation, the W-2 indicates the employer to be the Commission. Again, this further adds to the confusion as to whether the entities are separate.

The second contract, a rental contract signed in November 2000, is for the Foundation to sublease 968 square feet from the Commission for \$1,000 monthly. Based on the accounting records, the Commission allocated and billed the Foundation 50% of the full building rent, which is between \$4,392 - \$4,656 monthly and approximately 400% more than the agreed-upon terms. There appears to be no amendment to this contract to indicate any change in the agreed-upon terms. The Foundation is contractually bound to pay only \$1,000 monthly and the remainder of the rent expense may be the responsibility of the Commission. As a result, the Commission under-allocated the rent expense for itself and may not be accurately reporting this expense. When expenses are not accurately reported per the contract, one may not be able to rely on the financial statements as an effective analytical tool.

Cost Allocation

The Commission was unable to provide documentation for the methodology applied in the determination of the allocation rate when charging the Foundation for the shared expenses. Based on the type of expense, various allocation rates were used. For instance, in 2007/2008 fiscal year, 50% of rent, utilities, and janitorial services expenses and 20% of the copier lease were allocated to the Foundation. Without clear documentation, we are unable to determine whether the allocation rates used were reasonable. The Commission should maintain documentation demonstrating that management used estimated or actual data to determine the allocation and justifying the reason for using such data for the determination.

Accounting for Revenues and Expenses

There were instances when the Commission collected and deposited revenues for the Foundation's Zinfest event. The revenues were from ticket sales paid by attendees' credit cards or checks. These revenues were deposited into the Commission bank account because the credit card machine used to process the transactions was linked to the Commission bank account and the checks were paid to the order of the Commission. We noted that Zinfest revenues the Commission collected were not always paid in full to the Foundation; instead, the revenues offset the Zinfest accounts receivable balance. This balance consisted of the Zinfest expenses the Commission paid upfront. Additionally, there was a lack of clear documentation to determine the amounts netted. As a result, there was no transparency of the revenues and expenses, and we are concerned as to whether these revenues and expenses were accurately reflected in both entities' financial statements, since there could be a possibility that items were not properly classified to the correct entity. We further noted that these transactions were performed by the Commission's prior accountant and the current accountant indicated that the revenues and expenses will no longer be netted.

Classification of Direct Foundation Expenses

The expenses the Commission paid upfront for the Foundation were not always classified to the correct entity. We noted when no supporting documentation was provided or when the expense was not clearly identified as a Foundation expense, the expense was considered a Commission expense. During our fieldwork, the Commission requested vendor copies for the expenses which had no supporting documentation. From this subsequent documentation, the Commission determined these expenses were for Zinfest but were never reimbursed by the Foundation. For instance, we noted the Commission paid \$594 for wine purchased from the Visitor Center. There was no documentation justifying the expense and upon further research the Commission determined that it was a Zinfest expense. As a result, the Commission paid for this expense and Zinfest was never charged. Consequently, due to our finding, the Commission has invoiced the Foundation for this wine purchase and included it in the accounts receivable for fiscal year 2007/2008. Without clear documentation and proper review of the expenses, there is no assurance that Commission was reimbursed for all Foundation expenses. The Commission has reported and paid for Foundation expenses and as a result it did not properly report the expenses in its financial records.

Commission's Contribution to the Foundation

The Commission contributes money to the Foundation without requesting an accounting to ensure the money was used to benefit its mission. Additionally, the administrative contract does not mention the Commission is to provide direct financial support to the Foundation. We noted the Commission financially supported the Foundation's Visitor Center and Zinfest by absorbing the expenses that the Commission originally paid either through lowering the amount the Foundation owed monthly to the Commission or by not seeking reimbursement from them. This contribution was between 9% and 21% of the Foundation's annual income.

The Commission provided contributions to the Foundation for the Visitor Center and Zinfest. The Visitor Center received between \$85,000 and \$100,000 annually, which was

approximately 35% to 60% of the total Visitor Center expenses the Commission paid upfront. The Board approved and earmarked \$100,000 for fiscal year 2005/2006 and \$85,000 for each fiscal year 2006/2007 and 2007/2008; or \$8,333 and \$7,083 per month, respectively. The contribution of \$8,333 or \$7,083 per month was deducted from the total monthly expenses the Commission paid upfront for Visitor Center expenses, which reduced the amount owed to the Commission. As of June 30, 2008, the Visitor Center accounts receivable balance was \$112,336. It does not appear the Visitor Center paid on a consistent basis since invoices remained outstanding from October 2007.

Additional financial support totaling \$49,936 for Zinfest occurred only in fiscal year 2005/2006; however, the Board minutes did not mention any approval of this contribution. The \$49,936 contribution to Zinfest consisted of a \$28,000 check to the Foundation, paid after the event and documented as a “loan.” It does not appear the \$28,000 “loan” was ever repaid. We are unable to determine how this money was used without auditing the Foundation’s books and records or requesting an accounting of the “loan” to ensure the money was to benefit the Commission’s mission. The remaining \$21,936 was the balance of the Commission’s accounts receivable for Zinfest expenses the Commission paid upfront. This consisted of a one-time entertainment deposit of \$10,000 and recurring expenses for the website, office supplies, copier lease, advertisement, and postage. As of June 30, 2008, the accounts receivable balance for Zinfest was \$1,136.

Recommendations

- 1. The Commission should examine and revise its procedures to ensure there is clear separation, in fact and appearance, and ensure commingling of funds does not occur.*
- 2. The Commission should ensure that it is in compliance with its contracts between itself and the Foundation. If necessary, the contracts should be reviewed and amended.*
- 3. The Commission should review the costs associated with providing services to the Foundation and adopt a full cost recovery policy to ensure its full costs are recovered when performing services for the Foundation.*
- 4. The Commission should require its employees to maintain detailed time records that specifically identify the amount of time its employees spend performing Foundation activities in order to ensure the commingling of costs does not occur and to promote accuracy of the Commission’s financial statements.*
- 5. The Commission should maintain documentation demonstrating its analytical process and justification for using estimated data instead of actual data.*
- 6. The Commission should ensure that it retains supporting documentation for all accounting transactions.*
- 7. The Commission and the Foundation should ensure the direct expenses of each entity are properly recorded in each separate entity’s accounting records. If necessary, a policy should be developed to identify events, as either a Commission or Foundation activity.*
- 8. The Commission should seek reimbursement from the Foundation for any of the expenses that were not repaid.*

9. *The Commission should have the Foundation provide a full accounting for the \$28,000 “loan” that the Commission later noted as a contribution for Zinfest, to ensure all expenses further the mission of the Commission. Furthermore, the Commission should consider requiring recipients of large contributions to provide an accounting of the money to ensure it further the Commission’s mission.*

RELATIONSHIP WITH THE LODI CONFERENCE AND VISITORS BUREAU

A detailed review of the related documents identified internal control weaknesses in the relationship between the Commission and the Lodi Conference and Visitors Bureau (Visitors Bureau). The Visitors Bureau’s purpose is to market Lodi as an agri-tourism destination and conference venue. According to Commission staff, prior to 2005, the Visitors Bureau was a Commission program; the Commission provided one-third of the funding and the City of Lodi provided the remainder of the funding. In January 2005, the hotel tax was established to fund the Visitors Bureau; therefore, the Commission no longer needed to fund the Visitors Bureau. Due to our audit period beginning July 1, 2005, we did not review any of the expenses prior to this date. . Since January 2005, the Visitors Bureau separated from the Commission and became its own entity. At that time, the Commission did not establish a written contract with the Visitors Bureau and there was not sufficient supporting documentation for us to determine how the allocations for the reimbursement of the shared expenses were derived

After the Visitors Bureau separated from the Commission, the Bureau continued to occupy space without paying rent to the Commission. Instead, the Commission paid the full amount of rent and identified the Bureau’s portion as a “contribution” in their financial records. The “contribution” amounted to \$24,114. The Bureau did reimburse the Commission for other shared expenses such as utilities, office supplies, and a copier lease, for the period of July 1, 2005 through November 2005. However, the Commission did not receive reimbursement for these shared expenses from December 2005 through May 2006. Therefore, the Commission established an accounts receivable of \$1,465 for this amount owed. The Commission later reclassified the receivable as an expense and did not seek reimbursement. We also noted there were Board minutes indicating that the Commission would allow the Visitors Bureau to remain at Commission offices at no charge.

Furthermore, there was no documentation for the methodology used to determine the allocation rate for the shared expenses. Without supporting documentation, we are unable to determine whether the allocation rate applied was reasonable. The Commission should maintain documentation demonstrating that management used estimated or actual data to determine the allocation, and justifying the reason for using such data to determine the allocation.

Recommendations

10. *The Commission should consider establishing an accounts receivable for any unpaid amounts due and also ensure all business relationships are solidified in written contracts identifying the parties involved, terms for the performance, payment, scope, and signed by both parties.*

11. The Commission should maintain documentation demonstrating its analytical process and justification for determining the cost allocations between the two entities. Our office encourages the use of actual data to determine the allocation in order to provide a more accurate allocation.

LACK OF SUPPORT FOR EXPENSES

A review of the expenditures revealed lack of supporting documentation for credit card charges and/or a lack of a thorough review of expenses.

A Commission credit card was issued to a manager to facilitate business related expenses. Our office examined charges on the monthly credit card statements for supporting documentation and justifications. The Commission's travel policy adopted June 2008 requires expenses in excess of \$25 be accompanied by an original receipt for reimbursement. For the three-year period audited, our office noted \$32,950 of \$71,451, or 46% of expenses in excess of \$25 charged to the credit card were not adequately supported with receipts and/or justifications. Prior to June 2008, the Commission indicated the necessity to retain the itemized receipt was not apparent. During our fieldwork, we requested the Commission to obtain hotel invoices and any other receipts not originally provided in an attempt to reduce the total expenses charged without any supporting documentation. Furthermore, we noted the Commission did not readily have available a listing of the recipients of meals charged to the Commission, the business purpose for those meals, and the itemized receipt for restaurant charges. Without an itemized receipt that provides transparency to the nature of the expense, our office cannot attest to the reasonableness of the expenditure.

Our office further noted the Commission did not thoroughly review expenses prior to the processing of payment, which resulted in overpayments. The first instance occurred when the Commission paid Zinfest twice for the Zinfest related revenue the Commission collected. Zinfest did not repay the overpayment to the Commission; instead it created a credit of approximately \$2,476 at the Visitor Center, which was offset by the wine purchases for various promotional/marketing purposes. The second instance occurred when an employee's travel reimbursement was paid twice. An employee submitted a claim totaling \$1,385 for hotel and airfare expenses twice and both were paid in full without original receipts to support the expense. In reviewing the claim, the Commission should not have reimbursed the employee for either of the claims since it did not follow the travel policy regarding original receipts for expenses in excess of \$25. Payments of expenses should be examined to avoid double payments and ensure compliance with the Commission's internal policy prior to processing the payment.

Additionally, we noted a few instances of alcohol purchased that were not for wine, which do not appear to further the Commission's mission of promoting wine. We acknowledge the nature of the Commission's business and therefore have only noted alcohol purchases other than wine.

Recommendations

- 12. The Commission should ensure employees with a Commission issued credit card are required to support all charges incurred, including business meals, with an itemized receipt. The receipt should be maintained within the credit card file along with documentation listing the guests who attended and the business purpose of the meal.*
- 13. The Commission should incur expenses only necessary to support its mission.*
- 14. The Commission should maintain itemized receipts for all expenses to ensure expenses are adequately supported.*
- 15. The Commission should thoroughly review expenses prior to payment to avoid potential overpayments.*
- 16. The Commission should review employee travel claims to ensure the claim complies with the Commission's travel policy prior to reimbursement.*

LACK OF ACCOUNTABILITY WITH THE WINE INVENTORY

The lack of accountability over the wine inventory exposes the Commission to loss. The employees indicated that the Commission does not track the wine inventory. This inventory is purchased directly from local vineyards and wineries or from the Visitor Center tasting room, or occasionally the Commission receives donations from various entities. Then, this inventory is donated to organizations for fundraisers, sponsorship events, and public relation purposes. The wine is also used in wine seminars and other functions which appear to further the Commission's mission. However, without tracking the wine inventory, the Commission does not have knowledge of the value of the inventory, number of bottles of wine purchased or received into the inventory, and number of bottles of wine the Commission donated or used. Additionally, there is no assurance that all the wine was either donated or used for purposes that may benefit the Commission, since the recipient, purpose, and value of the donation were not always documented. While some recipients of large wine donations provided a letter indicating the number of bottles received and the event, this was not a consistent practice.

Although we noted that the wine inventory purchased from the Visitor Center had supporting documentation on many occasions, we did note instances when the supporting documentation was not sufficient. Of the \$38,956 in wine purchases from the Visitor Center, we found instances totaling \$1,255 when the Commission was unable to recall the recipient and purpose of the purchase. There were also instances totaling \$2,254 when the Commission paid the Visitor Center without a detailed receipt indicating the items purchased. Additionally, we noted the Commission purchased wine totaling \$304 that was used as gifts for special occasions, such as employee birthdays and as farewell gifts. State law requires public money to be used to further a department's mission. The gifts provided to employees do not appear to benefit or further the mission of the Commission and may be considered a gift of public funds. Furthermore, we noted that this wine inventory is not reported in the Commission's financial statements.

Recommendations

- 17. The Commission should establish policies and procedures for its wine inventory to ensure proper valuation and documentation of the use of the wine inventory. The documentation of the use of the wine inventory should include the recipient, purpose, and valuation of the donation provided.*
- 18. The Commission should not pay for any invoice from the Visitor Center unless accompanied by a detailed receipt to ensure the purchase was indeed from a Commission employee and for a purpose that would further the Commission's mission.*
- 19. The Commission should be cautioned that gifts of public funds are prohibited.*

WEAKNESSES IN CONTRACTS

In addition to the contract issues indicated in the above sections, our office noted the Commission paid for services from individuals or companies without a written contract and any evidence of bidding. The services were for, but not limited to, design for artwork, advertising, guides, maps, signage, newsletters publications, and event planning. For example, in fiscal year 2005/2006, the Commission paid \$32,182 to a communications and marketing company to plan a one-time event. The \$32,182 consisted of, but not all inclusive of, event management, administrative fees, accounting fees, hotel conference room rental, design and printing of invitations and booklets. Without a written contract, the Commission subjects itself to unnecessary internal control weaknesses. Because the Commission sought out these services and has an expectation of the finished product, it would be beneficial for them to have this in a formal written contract so both parties know what is expected. We recommend the contract identify the parties involved and outline the term of performance, payment, and scope to mitigate any possible disputes.

Recommendation

- 20. The Commission should ensure all services are properly bid and have written contracts that identify the parties involved; outline the terms for performance, payment, and scope; and are signed by both parties to mitigate any disputes.*

WEAKNESSES IN RESEARCH GRANT CONTRACTS

The Commission provides between \$69,700 and \$78,900 annually in grants to various organizations for research involving soil and grapevines. Based on our analysis of the grants the Commission provided, our office noted the Commission does not require the grantees to provide progress reports or a final accounting over the grant money awarded to them. Instead, the Commission requires researchers to present their findings in a final research report for the final payment.

The Commission should hold the grantees more accountable for the funds awarded to ensure the funds are solely used for their intended purpose. Although a budget is included in the grant contract, the Commission should not solely rely on the budget to account for final expenses since the actual expenditures incurred by the grant recipient could vary

significantly from the budgeted amount. Our office recommends the Commission require grantees to provide progress reports and a final accounting for the grant funds awarded to them. Progress reports are useful analytical tools that provide more information regarding the status of the grant projects and could possibly identify any potential concerns or questions the Commission may have. In addition, a final accounting of actual expenses would allow the Commission to determine whether use of the grant award was for the intended purpose and whether any grant money remained unspent. Ultimately, these reports will improve internal controls by providing more transparency over expenditures incurred by the researchers.

Recommendation

- 21. The Commission should improve its internal controls over grant awards by requiring grantees to provide additional financial information, such as progress reports and a final accounting of expenses applied against the grant. The purpose of these reports is to improve the Commission's monitoring of grant awards and provide more transparency over actual expenditures billed by researchers to the grant contract.*

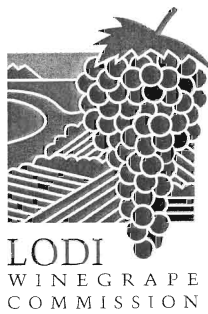
PERSONAL USE OF COMMISSION VEHICLES

The Commission has not accounted for or reported the value of the employees' use of the Commission's vehicles as a fringe benefit. The Commission owns two vehicles, a truck and a sport utility vehicle, which it allows two employees to use for personal and business use. Due to the lack of supporting documentation, we are unable to determine a monetary value of the benefit. Upon review of the two employees' payroll records and the IRS Form W-2, the value of the fringe benefit was not reported as income; only the employee's salary was reported as income.

Recommendation

- 22. The Commission should ensure that it is accounting for and reporting the income for the personal use of the Commission's vehicles by the two employees and determine whether the methodology complies with the IRS criteria in valuing the personal use the Commission's vehicle.*

LODI-WOODBRIDGE WINEGRAPE COMMISSION'S RESPONSE



December 17, 2008

Mr. Ron Shackelford, CPA
Chief, Audit Office
California Department of Food & Agriculture
1220 N Street, Room 344
Sacramento, CA 95814

Dear Mr. Shackelford:

I am writing in my capacity as Chairman of the Lodi Winegrape Commission (Commission) to respond to the preliminary draft audit of the Commission, and accompanying recommendations, provided to the Commission in documents dated November 4, 2008.

The Commission welcomes the opportunity provided by the audit to fine tune its administrative functions, policies and procedures, so that it is as efficient as possible in implementing its statutorily mandated responsibilities. It is with this mindset that the Commission's board of directors and staff have given full consideration to the audit and recommendations in preparation of the response which follows.

The Commission wants to point out that it has successfully conducted year end audits for the past seventeen years and the accounting issues addressed in your audit have never been raised before. Further, the Commission became aware of some auditing standards only in May, 2008, immediately before this audit was conducted. More importantly, it is our understanding that the California Department of Food and Agriculture is in the process of changing these standards or guidelines again.

It is important to understand that the Commission has, since its inception, attempted to maximize the educational component of its activities by entering into agreements with other organizations, including the California Wine Education Foundation and the Lodi Conference and Visitor's Bureau. These business relationships have allowed the Commission to leverage its resources in a manner consistent with its statutory authority and thereby provide significant benefit to persons subject to Commission law and to the people of California.

Mr. Ron Shackelford, CPA
California Department of Food and Agriculture
December 17, 2008
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The Commission has carried out its activities consistent with its governing law (Food & Ag. Code §§ 74801 et seq.) and the Policies for Marketing Programs manual issued by CDFA.

In closing, I want to share with you the appreciation of Commission staff for the professional manner in which you and your staff have conducted the audit. Please contact me at your convenience if you would like additional explanation regarding the Commission's response to the audit and recommendations.

Sincerely,

A handwritten signature in black ink, appearing to read "Keith Watts", written in a cursive style.

Keith Watts, Chairman

CDFA AUDIT RECOMMENDATIONS AND COMMISSION RESPONSES

1. *The Commission should examine and revise its procedures to ensure there is clear separation, in fact and appearance, and ensure commingling of funds does not occur.*

The Commission will make the changes necessary to ensure appropriate administrative and financial separation between the not-for-profit California Wine Education Foundation (Foundation) and the Commission, including the use of separate credit cards, improved time records, drafting new or revising existing contracts and other necessary changes. These changes are underway. Credit Cards for the Foundation are in process as is a policy and system for time keeping among employees. Existing contracts between the Foundation and the Commission shall be reviewed and revised to accurately reflect the duties and obligations of the parties. New contracts will be drafted for joint events, such as Zinfest to clearly address the rights and obligations of the parties. The Commission anticipates many of these items will be completed by mid year 2009.

2. *The Commission should ensure that it is in compliance with its contracts between itself and the Foundation. If necessary, the contracts should be reviewed and amended.*

The Commission agrees and as stated above, existing contracts between the Foundation and the Commission shall be reviewed and revised to accurately reflect the duties and obligations of the parties. If necessary, new contracts will be drafted to address joint events such as Zinfest. The Commission believes this process will be completed by mid year 2009.

3. *The Commission should review the costs associated with providing services to the Foundation and adopt a full cost recovery policy to ensure its full costs are recovered when performing services for the Foundation.*

The Commission agrees that the rental agreement and administrative services agreement should be revised to provide more specificity as to the duties and obligations of the Commission and the Foundation. In reviewing and revising these documents, the Commission will ensure that its employees are fully compensated for services provided to the Foundation and will include a provision to address recovery of overhead costs as well. The Commission believes this process will be completed by mid year 2009.

4. *The Commission should require its employees to maintain detailed time records that specifically identify the amount of time its employees spend performing Foundation activities in order to ensure the commingling of costs does not occur and to promote accuracy of the Commission's financial statements.*

The Commission agrees that it is prudent to establish a system for tracking time employees spend performing Foundation activities. The Commission staff is currently developing a system for this purpose. This will be reflected in the revision or amendment to the administrative services agreement. Further, with events such as Zinfest, a contract will be prepared that defines the responsibilities and duties of each entity that will cover Commission employee services.

5. *The Commission should maintain documentation demonstrating its analytical process and justification for using estimated data instead of actual data.*

The Commission agrees that actual data should be the basis for cost allocation between the Commission and the Foundation and the administrative services agreement shall be reviewed and revised or amended where necessary to address this.

6. *The Commission should ensure that it retains supporting documentation for all accounting transactions.*

The Commission agrees and has implemented this recommendation.

7. *The Commission and the Foundation should ensure the direct expenses of each entity are properly recorded in each separate entity's accounting records. If necessary, a policy should be developed to identify events, as either a Commission or Foundation activity.*

The Commission and the Foundation have maintained separate accounts since their existence. The Commission staff is currently reviewing this process and developing a more detailed accounting method. The Commission believes this process will be completed by mid year 2009.

8. *The Commission should seek reimbursement from the Foundation for any of the expenses that were not repaid.*

The Commission has an outstanding Account Receivable with the Foundation. The Commission anticipates that this outstanding amount will be resolved by June, 2009. As indicated in the Commission's response to preceding recommendations #1-7, the Commission will ensure that effective policies are in place to account for and recover all

expenses incurred in providing services for the Foundation and other business relationships.

9. *The Commission should have the Foundation provide a full accounting for the \$28,000 "loan" that the Commission later noted as a contribution for Zinfest, to ensure all expenses further the mission of the Commission. Furthermore, the Commission should consider requiring recipients of large contributions to provide an accounting of the money to ensure it further the Commission's mission.*

The Commission understands the value and necessity of ensuring that these funds further the Commission's mission and that the Commission be fully informed and provided an accounting of these funds. The Commission understands that because CDFA does not audit the Foundation's books there may be some misunderstanding regarding these funds. The Commission and the Foundation work together on Zinfest and as a result, the Commission is fully advised of the use of these funds and that their use furthered the mission of the Commission. This amount was used for advertising and printing costs to promote Zinfest.

As stated above in response to recommendations #1-8, the Commission is revising its procedures with respect to Zinfest and the Commission will ensure that effective policies are in place as well as appropriate contractual relationships to account for the exchange of money and services regarding this event.

10. *The Commission should consider establishing an accounts receivable for any unpaid amounts due and also ensure all business relationships are solidified in written contracts identifying the parties involved, terms for the performance, payment, scope, and signed by both parties.*

The Commission understands the necessity of ensuring all business relationships are solidified with written contracts with specificity towards the rights and obligations of the parties. As indicated in responses to recommendations #1-9 above, the Commission is reviewing, revising, amended and drafting contracts and policies to ensure this policy is in effect moving forward.

With respect to the Lodi Conference and Visitors Bureau (Visitors Bureau), the Commission and Visitors Bureau separated in January 2005 and no written contract was established moving forward. It was the intention of the Commission that the relationship end at that time, but the Visitors Bureau took some time in their relocation effort. As CDFA is no doubt aware, the statute of limitations has passed for seeking reimbursement of these funds. Further, even if this were not the case, the Commission agreed by Board

resolution to allow the Visitors Bureau to remain at the Commission offices without paying rent during this time of transition. The Board assessed the situation and determined it was in the best interest of the Commission to allow for this transition, rather than incur the cost of removing the Visitors Bureau and seeking compensation. While a CDFA representative did not attend this meeting, minutes were reviewed by CDFA and no mention was made that this was inappropriate.

This action would clearly be considered accord and satisfaction if the Commission were to pursue reimbursement. Since there are clear legal barriers to such action, the Commission believes that this would not be in the best interest of the Commission. On a going forward basis, however, the Commission shall ensure a full cost recovery policy for future business relationships.

11. *The Commission should maintain documentation demonstrating its analytical process and justification for determining the cost allocations between the two entities. Our office encourages the use of actual data to determine the allocation in order to provide a more accurate allocation.*

The Commission agrees and as stated above in response to recommendation #5, the Commission shall utilize actual data in determining cost allocation in its business relationships.

12. *The Commission should ensure employees with a Commission issued credit card are required to support all charges incurred, including business meals, with an itemized receipt. The receipt should be maintained within the credit card file along with documentation listing the guests who attended and the business purpose of the meal.*

The Commission agrees with this recommendation and has implemented this procedure.

13. *The Commission should incur expenses only necessary to support its mission.*

The California legislature has determined that it is in the public interest that the public be made aware of accurate and scientific information relating to the beneficial qualities of winegrapes and winegrape products. Cal. Gov. Code sec. 74803.

Further, the legislature specifically found that opportunity exists for continued growth and expansion of the industry and the success of an expansion program is uniquely dependent upon effective market development, promotion, and research. In addition, the expansion of the winegrape industry also provides an important source of jobs for many

people in this state, a high proportion of whom reside in historically depressed areas of the state. Cal. Gov. Code sec. 74807.5

The Commission has always acted in the best interest of the public welfare and in support of this mission. CDFA's concern appears to focus on the issue of documentation rather than inappropriate use of funds. Some clarification is therefore required.

In May, 2008, CDFA advised marketing programs that it would now require itemized receipts and additional documentation for expenses. A credit card receipt would no longer be considered acceptable back up. In response, the Commission quickly adopted a new policy and going forward is providing additional documentation as requested by CDFA. The audit period, however, is retroactive and as observed, it is difficult to retrace three years worth of back up documentation.

The Commission welcomes the guidance provided by CDFA and as demonstrated is quickly implementing new policies on its own initiative and in response to CDFA recommendations. To imply, however, that the Commission is incurring expenses outside of its mission because CDFA is implementing standards retroactively leaves a false impression that could be misinterpreted in reviewing these recommendations.

14. The Commission should maintain itemized receipts for all expenses to ensure expenses are adequately supported.

The Commission agrees and as stated in response to recommendation #12 has implemented this policy.

15. The commission should thoroughly review expenses prior to payment to avoid potential overpayments.

The Commission agrees and has already implemented this policy. It should be noted that the overpayment was repaid immediately upon discovery.

16. The Commission should review employee travel claims to ensure the claim complies with the Commission's travel policy prior to reimbursement.

The Commission agrees with this recommendation and as CDFA mentions, a new policy was implemented in June, 2008. The travel claim reimbursement CDFA references was resolved quickly upon discovery and the Commission has implemented new procedures to effectively address this concern.

17. *The commission should establish policies and procedures for its wine inventory to ensure proper valuation and documentation of the use of the wine inventory. The documentation of the use of the wine inventory should include the recipient, purpose, and valuation of the donation provided.*

The Commission agrees and is establishing an inventory which shall include the information requested by CDFA. The Commission anticipates that this inventory shall be complete by midyear 2009.

18. *The Commission should not pay for any invoice from the Visitor Center unless accompanied by a detailed receipt to ensure the purchase was indeed from a Commission employee and for a purpose that would further the Commission's mission.*

The Commission agrees and has already implemented a new procedure to track these purchases and provide oversight for the purchase.

19. *The Commission should be cautioned that gifts of public funds are prohibited.*

The Commission understands the nature of its funding and its source. As stated above in response to recommendation #13, the Commission has always acted in support of its mission and in the public interest and will continue to do so.

CDFA references the purchase of wine totaling \$304 over a three year period as gifts for special occasions. This is roughly \$100.00 per year. As was recently demonstrated at a CDFA marketing meeting, the Commissions were not aware that de minimus items awarded to employees for their efforts in support of the Commission mission and the public interest would be considered a gift of public funds. These items were not "free" but were a response to effort exceeding their employment duties.

The Commission is currently investigating different options of addressing employee compensation and benefits and will address this issue as part of that process.

20. *The Commission should ensure all services are properly bid and have written contracts that identify the parties involved; outline the terms for performance, payment and scope; and are signed by both parties to mitigate any disputes.*

The Commission agrees that written contracts are appropriate and has acted to enter into contracts with certain vendors. There are some situations where the amount involved is minor and expediency is an issue when a written contract is not efficient.

On May 3, 2007, a memorandum was issued to all program executives by CDFA addressing the scope and requirements of the fiscal compliance audits the Marketing Branch was initiating. With respect to contracts, the memorandum (attached) stated as follows:

“Failure to competitively evaluate contractors (but note, if there is a competitive evaluation documented, a board not following the specifics of the State Administrative Manual (SAM), the Personnel Administrative Manual (PAM), and Department of Personnel Administration (DPA) guidelines is not relevant or reportable)”.

CDFA has recently (November, 2008) provided additional guidance with respect to contracts and Requests for Proposals (RFP). It should be noted, however, that these guidelines do not identify what contract amount or other circumstances trigger the need for a bid. Instead, the guidelines request the Commission to bid contracts, “wherever possible”.

The Commission shall strive to implement these regulations and at a minimum will ensure that written contracts are created and maintained. These contracts will address the duties and responsibilities of the parties including terms of performance, payment and scope. In situations where urgency or a small dollar amount is involved, the Commission shall implement a procedure to provide written documentation and support for compensation prior to payment.

Because of the Commission’s size and the time involved with bidding, the Commission will identify a bidding process or functional equivalent (such as an RFP) and implement this with larger contracts. If a bidding process is not used, an explanation will be provided. The Commission will implement a policy to review contracts annually.

21. *The Commission should improve its internal controls over grant awards by requiring grantees to provide additional financial information, such as progress reports and a final accounting of expenses applied against the grant. The purpose of these reports is to improve the Commission’s monitoring of grant awards and provide more transparency over actual expenditures billed by researchers to the grant contract.*

The Commission agrees and asserts that it has requested and been provided with progress reports for its research grants. In addition, the Commission has always requested and received a final accounting of these expenses.

22. *The Commission should ensure that it is accounting for and reporting the income for the personal use of the Commission's vehicles by the two employees and determine whether the methodology complies with the IRS criteria in valuing the personal use the Commission's vehicle.*

The Commission agrees with this recommendation and has implemented the methodology in compliance with IRS criteria.

CDFA EVALUATION OF RESPONSE

A draft copy of this report was forwarded to the management of the Lodi-Woodbridge Winegrape Commission, for its review and response. We reviewed the response and it satisfactorily addresses the findings in this report.

DISPOSITION OF AUDIT RESULTS

The findings in this report are based on fieldwork my staff performed August 4, 2008 through August 22, 2008. My staff met with management on August 22, 2008 to discuss the findings and recommendations, as well as other issues.

This report is intended for the CDFA and the Commission for their review and action if necessary. However, this report is public document and its distribution is not restricted.

REPORT DISTRIBUTION

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1	Chief Executive Officer, Lodi-Woodbridge Winegrape Commission
1	Director, CDFA Marketing Services Division
1	Branch Chief, CDFA Marketing Branch
1	Chief Counsel, CDFA Legal Office
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